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CITATIONS

273952—40

Miscellaneous:

In the Supreme Court of the United States

OCTOBER TERM, 1940

No. 113

CHESTER GAINES AND THERESA GAINES, HUSBAND AND WIFE, PETITIONERS

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The memorandum opinion of the Board of Tax Appeals (R. 15) is unreported. The *per curiam* opinion of the Circuit Court of Appeals (R. 27) is reported in 111 F. (2d) 144.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered May 8, 1940. (R. 27–28.) The petition for a writ of certiorari was filed May 29,

1940, and was granted October 14, 1940. The jurisdiction of this Court is conferred by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether, under the Revenue Act of 1934, the filing of a joint return permits the wife's capital losses to be deducted from her husband's capital gains.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix *infra*, pp. 9–12.

STATEMENT

The facts, as stipulated (R. 23–24), may be summarized as follows:

The petitioners were married and living together as husband and wife throughout the calendar year 1934. During that year the husband, Chester Gaines, realized a net gain from the sale of capital assets of $18,466.41, the entire amount of which was to be taken into account under Section 117 (a) of the Revenue Act of 1934. During the same year his wife, Theresa Gaines, sustained a net loss from the sale of capital assets of $35,959.86, of which the amount to be taken into account under Section 117 (a) of the Revenue Act of 1934 was $20,031.59.

The petitioners filed a joint income tax return for 1934, in which they reported a capital loss of \$1,565.18, which represented the difference between the husband's net capital gain taken into account (\$18,466.41) and the wife's net capital losses taken into account (\$20,031.59).

In auditing the return, the Commissioner held that the losses sustained by the wife could not be applied to reduce the gains realized by the husband, and that the wife's losses accordingly could be deducted only to the extent of her own gains, plus \$2,000. By reason of this holding, the Commissioner added \$18,031.59 to the net income reported by the petitioners. On the basis of this adjustment, the Commissioner determined a deficiency of \$5,008.55 (R. 13).

The Board of Tax Appeals sustained the Commissioner's determination (R. 16). The Circuit Court of Appeals affirmed (R. 27), *per curiam,* the order of the Board, upon the authority of that court's decision in *Pierce* v. *Commissioner,* 100 F. (2d) 397. This Court granted certiorari (R. 29).

ARGUMENT

The question presented in this case is precisely the same as that in *Helvering* v. *Janney,* No. 36, this Term, to be argued immediately preceding this case. Both cases arise under the Revenue Act of 1934. Hence, we adopt for this case the brief on behalf of the Commissioner of Internal Revenue in the *Janney* case. Here we discuss only those of

the arguments advanced by the petitioners which are not covered in the brief for the Commissioner in the *Janney* case.

1. The petitioners' principal argument in the present case is that prior to enactment of the Revenue Act of 1932 the right of husband and wife to pool their losses in a joint return embraced the right here claimed, that Congress had no purpose "to diminish this prior privilege" by the insertions of Section 23 (r) (1) in the 1932 Act and 117 (d) in the 1934 Act, and that the adoption of the provisions hence did not justify the Treasury in promulgating regulations in derogation of the "prior privilege." But the specific question here at issue arose only with the enactment of Section 23 (r) (1) of the 1932 Act, providing that losses from sales or exchanges of stocks and bonds held by the taxpayers for less than two years should be allowed only to the extent of gains from such sales or exchanges.[1] And so far as that question was determinable according to general principles, the predecessors of Article 51-1 of Regulations 86, providing that if

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[1] "There are no provisions in existing law corresponding to Section 23 (r), (s), and (t)." S. Rept. No. 665, 72d Cong., 1st Sess., p. 17.

The petitioners apparently suggest (Br. 10, note 2) that the question at bar arose under Section 208 (c) of the 1924 Act and its successors (Revenue Act of 1926, Section 208 (c); 1928, Section 101 (b); 1932, Section 101 (b)), and that the right here claimed by the taxpayers was accorded in the administration of that provision. Section 208 (c) provided that in the case of any taxpayer who sustained a capital net loss (i. e. a loss from the sale or exchange of property held

a joint return were filed the tax should be computed on the aggregate income and that all deductions "to which either is entitled" should be taken from such aggregate income, gave notice that it was the Treasury's general position that before any deduction might be entered in a joint return it must be a deduction to which either the husband or the wife, separately considered, was entitled under the law.

2. In *Pierce* v. *Commissioner,* 100 F. (2d) 397 (C. C. A. 2d), and in the brief for the Commissioner in the *Janney* case, various decisions are referred to in support of the proposition that even though husband and wife file a joint return "each is treated as a separate individual who can carry deductions into the joint return only in his or her

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for more than two years) the tax should be determined by computing a tax upon the ordinary net income at the usual rates and by deducting from this tax 12½ per centum of the capital net loss. This section further provided that in no case should the tax computed under it be less than the tax computed without reference to it. Because of the provision last referred to, Section 208 (c) was operative only with respect to capital losses which would otherwise have been offset against income taxable at the rate of 12½ per centum or more. Section 208 (c) was correlative to Section 208 (b), which permitted a taxpayer to elect that his net capital gain be taxed at the rate of 12½ per centum instead of at the rate otherwise applicable.

Section 208 (c), unlike the statutory provisions involved here and in the *Taft* case No. 183, argued herewith, did not make the amount of or the right to the deduction contingent upon the amount or kinds of income of the taxpayer. Hence it was unnecessary to the policy of the Section that one spouse be prohibited from deducting the capital losses of the other; there was no more reason to prohibit the pooling of such deductions than of other deductions.

own right" (100 F. (2d) at 398). Petitioners assert that the decisions so refered to do not support the proposition for which they are cited, and, at the same time, that the position unsuccessfully taken by the Commissioner in some of these cases was inconsistent with his present position. We think, on the other hand, that the positions taken in those cases were not inconsistent with the present position of the Treasury, for the reason that those cases presented special considerations which might have removed them from the operation of the principle that a husband and wife remain separate individuals for the purpose of computing their deductions even though they file a joint return. And certainly the cases stand for this principle, since the courts refused to exclude them from its scope, despite the presence of factors which might have induced the courts to do so.

The earliest of these cases is *Frank B. Gummey* v. *Commissioner,* 26 B. T. A. 894 (1932). There the Board held that husband and wife were to be treated as separate individuals for purposes of the "wash" sale provision, i. e., that a deduction might be taken in a joint return for losses sustained by one spouse on the sale of securities even though the other spouse brought similar securities immediately thereafter.[2] Similarly held that losses

[2] The Bureau acquiesced in this decision, XIII-2 Cum. Bull. 8, and overruled its prior ruling to the contrary. I. T. 2824, XIII-2 Cum. Bull. 293, overruling I. T. 1997, III-1 Cum. Bull. 149.

stained by one spouse in a bona fide sale of securi-
es to the other spouse could be deducted in a joint
turn. *Commissioner* v. *Thomas,* 84 F. (2d) 562
C. C. A. 5th); *Joseph E. Uihlein* v. *Commissioner,*
) B. T. A. 399 affirmed *sub nom Commissioner* v.
rumder, 82 F. (2d) 944 (C. C. A. 7th); *Hill* v.
nited States, 12 F. Supp. 798 (C. Cls.). In those
ses a contrary result might well have been
eached as necessary to prevent tax evasion, with-
ut abandoning the position that husband and wife
re not, as a general proposition, to be treated as
single taxpayer even if they file a joint return.
t was to close the avenue of tax evasion opened by
hese decisions, and not as an outgrowth of any
ngle taxpayer theory, that Congress provided in
ection 24 (b) (1) of the Revenue Act of 1938 that
o deductions should be allowed for losses result-
ng from sales between members of a family.[3]
ee H. Rep. No. 704, 73d Cong., 2d Sess., p. 23;
939-1 Cum. Bull. 554, 571; 78 Cong. Rec. 2662.
ee also (1940) 53 Harv. L. Rev. 681, 682; (1940)
9 Yale L. J. 1279, 1283. The position taken by
he Bureau in those cases was thus not inconsistent
vith, and the holdings of the courts support, its
osition here.

Similarly the position taken by the Commis-
ioner that spouses filing a joint return were

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[3] Whether this amendment reaches the question which was
resented in the *Gummey* case, or only that involved in the
homas, Brumder, and *Hill* cases, is not clear. See (1940)
9 Yale L. J. 1279, 1283, note 35.

jointly and severally liable for the tax was necessary as a matter of administration, because of the difficulty of determining the proportion of the tax liability attributable to each spouse. Congress so recognized in inserting in Section 51 (b) of the 1938 Act a provision explicitly making liability for the tax joint and several. See H. Rept. No. 1860, 75th Cong., 3d Sess., pp. 29–30. But the cases rejecting the Commissioner's contention support the view that a husband and wife remain separate taxpayers even though they file a joint return. *Cole* v. *Commissioner,* 81 F. (2d) 485, 487 (C. C. A. 9th); *Crowe* v. *Commissioner,* 86 F. (2d) 796 (C. C. A. 7th); *Commissioner* v. *Rabenold,* 108 F. (2d) 639 (C. C. A. 2d).

CONCLUSION

For the reason stated in the brief for the Commissioner in the *Janney* case and herein it is submitted that the judgment of the court below should be affirmed.

Respectfully submitted.

Robert H. Jackson,
Attorney General.
Samuel O. Clark, Jr.,
Assistant Attorney General.
Sewall Key,
Maurice J. Mahoney,
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Special Assistants to the Attorney General.

November 1940.

APPENDIX

Revenue Act of 1934, c. 277, 48 Stat. 680:

SECTION 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(j) *Capital Losses.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent provided in section 117 (d).

* * * * *

(U. S. C., Title 26, Sec. 23.)

SEC. 51. INDIVIDUAL RETURNS.

* * * * *

(b) *Husband and Wife.*—If a husband and wife living together have an aggregate net income for the taxable year of $2,500 or over, or an aggregate gross income for such year of $5,000 or over—

(1) Each shall make such a return, or

(2) The income of each shall be included in a single joint return, in which case the tax shall be computed on the aggregate income.

* * * * *

(U. S. C., Title 26, Sec. 51.)

SEC. 117. CAPITAL GAINS AND LOSSES.

(a) *General Rule.*—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital

asset shall be taken into account in computing net income:

100 per centum if the capital asset has been held for not more than 1 year;

80 per centum if the capital asset has been held for more than 1 year but not for more than 2 years;

60 per centum if the capital asset has been held for more than 2 years but not for more than 5 years;

40 per centum if the capital asset has been held for more than 5 years but not for more than 10 years;

30 per centum if the capital asset has been held for more than 10 years.

* * * * *

(d) *Limitation on Capital Losses.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges. If a bank or trust company incorporated under the laws of the United States or of any State or Territory, a substantial part of whose business is the receipt of deposits, sells any bond, debenture, note, or certificate or other evidence of indebtedness issued by any corporation (including one issued by a government or political subdivision thereof), with interest coupons or in registered form, any loss resulting from such sale (except such portion of the loss as does not exceed the amount, if any, by which the adjusted basis of such instrument exceeds the par or face value thereof) shall not be subject to the foregoing limitation and shall not be included in determining the applicability of such limitation to other losses.

* * * * *

(U. S. C., Title 26, Sec. 101.)

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 51–1. *Individual returns.*—For each taxable year every single person and every married person not living with husband or wife for any part of the taxable year, whose gross income as defined in sections 22 and 116 is $5,000 or over, or whose net income as defined in section 21 is $1,000 or over, must make a return of income. Every married person living with husband or wife for any part of the taxable year, but not at the close of the taxable year, must make a return if his gross income for the taxable year is $5,000 or more, or his net income is equal to, or in excess of, the credit allowed him by section 25 (b) (1) and (3) (computed without regard to his status as the head of a family). (See article 25–7.) A husband and wife living together for the entire year need make no returns unless their aggregate gross income for the taxable year is at least $5,000, or their aggregate net income is at least $2,500. If their aggregate net income for the taxable year is $2,500 or more, or their aggregate gross income is $5,000 or more, either each must make a return, or the income of each must be included in a single joint return. A husband and wife living together at the close of the taxable year but not during the entire taxable year must make a return or returns if their aggregate gross income for the taxable year is $5,000 or more, or their aggregate net income is equal to, or in excess of, the credit allowed them by section 25 (b) (1) and (3). (Computed without regard to the status of either of them as the head of a family.) (See article 25–7.) If the income of each is included in a single joint return, the tax is

computed on the aggregate income and all deductions and credits to which either is entitled shall be taken from such aggregate income. A joint return of husband and wife may be filed only if they were living together at the close of their taxable year. If one spouse dies prior to the last day of the taxable year, the surviving spouse may not include the income of the deceased spouse in a joint return for such taxable year.

* * * * *

ART. 117-5. *Application of section 117 in the case of husband and wife.*—In the application of section 117, a husband and wife, regardless of whether a joint return or separate returns are made, are considered to be separate taxpayers. Accordingly, the limitation under section 117 (d) on the allowance of losses of one spouse from sales or exchanges of capital assets is in all cases to be computed without regard to gains and losses of the other spouse upon sales or exchanges of capital assets.

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SUPREME COURT OF THE UNITED STATES.

Nos. 36 and 113.—October Term, 1940.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, 36 *vs.* Walter C. Janney and Pauline F. M. Janney.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.
Chester Gaines and Theresa Gaines, Petitioners, 113 *vs.* Guy T. Helvering, Commissioner of Internal Revenue.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[December 9, 1940.]

Mr. Chief Justice Hughes delivered the opinion of the Court.

These cases present the same question, that is, whether under the Revenue Act of 1934, in the case of a joint return by husband and wife, the capital losses of one spouse may be deducted from the capital gains of the other.

In *Helvering* v. *Janney,* the wife realized net gains from the sale of capital assets during 1934, and the husband realized net losses from the sale of capital assets during the same year. They filed a joint income tax return reporting the capital gain, which represented the difference between the wife's adjusted capital gains and the husband's adjusted capital losses. The Commissioner ruled that the husband's losses could not be applied to reduce the gains realized by his wife and accordingly determined a deficiency. The Board of Tax Appeals sustained the Commissioner (39 B. T. A. 240) but the Circuit Court of Appeals for the Third Circuit reversed. 108 F. (2d) 564.

In *Gaines* v. *Helvering,* the husband realized a net gain from the sale of capital assets during 1934, while his wife sustained a net loss from the sale of capital assets. They filed a joint return reporting a capital loss, which represented the difference between the husband's net capital gain and his wife's net capital loss. The Commissioner, as in the *Janney* case, decided against this adjustment and the Board of Tax Appeals affirmed. The Circuit Court of Ap-

peals for the Second Circuit affirmed the decision of the Board. 111 F. (2d) 144.

In view of the conflict between these decisions, we granted certiorari. No. 36, 310 U. S. 617; No. 113, October 14, 1940.

Section 51(b) of the Revenue Act of 1934[1] with respect to the returns of husband and wife provided:

"(b) Husband and Wife.—If a husband and wife living together have an aggregate net income for the taxable year of $2,500 or over, or an aggregate gross income for such year of $5,000 or over—

"(1) Each shall make such a return, or

"(2) The income of each shall be included in a single joint return, in which case the tax shall be computed on the aggregate income".

The same provision in substance is found in the earlier Revenue Acts from that of 1921.[2]

The "aggregate income", to which paragraph 2 of Section 51(b) refers, is clearly the aggregate net income as it is the aggregate income on which "the tax is to be computed". In that view the deductions to which either spouse would be entitled would be taken, in the case of a joint return, from the aggregate gross income.

That was the construction placed upon the provision for a joint return in the Revenue Act of 1918 by the Solicitor of Internal Revenue in an opinion rendered in 1921.[3] After considering the terms of the statute and the reasonable inference as to the intent of Congress, the Solicitor concluded:

"From the foregoing it follows that the proper construction of the Revenue Act of 1918 permits a husband and wife living together, at their option, to file separate returns or a single joint return. If a single joint return is filed it is treated as the return of a taxable unit and the net income disclosed by the return is subject to both normal and surtax as though the return were that of a single individual. In cases, therefore, in which the husband or wife has allowable deductions in excess of his or her gross income, such excess

1 48 Stat. 697.

2 The Revenue Act of 1918, Section 223, also provided for a joint return by husband and wife. 40 Stat. 1074.

Section 223(b) of the Revenue Act of 1921 provided (42 Stat. 250):

"(b) If a husband and wife living together have an aggregate net income for the taxable year of $2,000 or over, or an aggregate gross income for such year of $5,000 or over—

"(1) Each shall make such a return, or

"(2) The income of each shall be included in a single joint return, in which case the tax shall be computed on the aggregate income".

3 Sol. Op. 90, Cum. Bull. No. 4, p. 236 (1921).

may, if joint return is filed, be deducted from the net income of the other for the purpose of computing both the normal and surtax''.

The terms of the Revenue Act of 1921 made this view even clearer.[4] Treasury Regulations 62, Article 401, promulgated under the Revenue Act of 1921, apparently followed the same view. That article provided as to joint returns of husband and wife,—

''Where the income of each is included in a single joint return, the tax is computed on the aggregate income and all deductions and credits to which either is entitled shall be taken from such aggregate income''.[5]

The question as to deductions for losses on sales or exchanges of securities arose under Section 23(r)(1) of the Revenue Act of 1932.[6] That provided that losses as there described should be allowed only to the extent of gains derived from such sales or exchanges. Nothing was said in this section which in any way affected the provision of the statute as to joint returns by husband and wife. The question in that relation, that is, as to deduction for losses on sales of securities, was submitted to the Commissioner of Internal Revenue and was answered by him on December 29, 1932, as follows:

''The specific question presented is whether the loss sustained by the husband may be applied to offset the same amount of gain realized by the wife in rendering joint income tax return for the year. In reply you are advised that, in the case of a husband and wife living together who file a joint income tax return, the tax liability is computed on the aggregate income as provided by section 51(b)(2) of the Revenue Act of 1932, and such joint return is

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4 The Committee on Ways and Means of the House of Representatives reported with respect to the provision of the bill which became the Revenue Act of 1921 as follows:

''Section 231 of the bill proposes to amend Section 223 of the present law in such a manner as to clear up the doubt now existing as to the right of husband and wife in all cases to make a joint return and have the tax computed on the combined income''. House Rep. No. 350, 67th Cong., 1st Sess. See, also, Sen. Rep. No. 275, 67th Cong., 1st Sess.

5 The same provision was continued in substance in succeeding regulations. Article 401 of Treasury Regulations 65 and 69 under the Revenue Acts of 1924 and 1926; Article 381 of Regulations 74 and 77 under the Revenue Acts of 1928 and 1932.

6 47 Stat. 183. Section 23(r)(1) provided: ''Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations).

treated as if it was the return of a single individual. The aggregate income in such case would of course embrace the gains as well as the allowable deductions of each spouse. If it is correctly understood from your letter that the gains and losses in the illustration presented are from transactions falling within the same class within the meaning of the statute such as sales of securities not held for a period of more than two years, the loss sustained by the husband would offset the same amount of gain realized by the wife from such source".[7]

This statement by the Commissioner applied the same principle which had previously been followed with respect to deductions in the joint returns of husband and wife, there having been no indication by Congress of any different purpose.

Treasury Regulation No. 77, promulgated under the Act of 1932, contained nothing to the contrary and the regulation theretofore obtaining as to such joint returns was left unchanged. Art. 381.

The Revenue Act of 1934 continued the prior statutory provisions as to joint returns of husband and wife, and Section 117(d) of that Act, as to capital losses, did not purport to alter the rule as to the right of the spouses to deductions in their joint return. Section 117(d) merely limited the amount of losses which could be deducted, as follows:

"(d) *Limitation on Capital Losses.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges".

The conclusion of the Commissioner with respect to the Act of 1932, in the opinion above mentioned, was equally applicable to the new Act.

It was not until 1935 that the Treasury Department by Article 117-5 of Regulations 86 undertook to provide that "the allowance of losses of one spouse from sales or exchanges of capital assets is in all cases to be computed without regard to gains and losses of the other spouse upon sales or exchanges of capital assets".[8]

We are of the opinion that under the provision of the Act of 1934 as to joint returns of husband and wife, which embodied a policy set forth in substantially the same terms for many years, Congress intended to provide for a tax on the aggregate net income and that the losses of one spouse might be deducted from the gains of the

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7 1933 Commerce Clearing House Federal Tax Service, Vol. III, par. 6037.

8 It was also in 1935 that the Bureau of Internal Revenue announced the same ruling under the Act of 1932. G. C. M. 15438, Cum. Bull. XIV-2, p. 156.